



April 5, 2009

Michael E. Fryzel, Chairman  
Rodney E. Hood, Vice Chairman  
Gigi Highland, Board Member  
National Credit Union Administration  
1775 Duke Street  
Alexandria, VA 22314-3428

Re: Comments on Advanced Notice of Proposed Rulemaking – Part 704  
Sent via email to [regcomments@ncua.gov](mailto:regcomments@ncua.gov)

I am writing comments in response to the ANPR regarding the structure of the Corporate Network, Part 704, with the request that NCUA take every precaution so as not to make such broad, sweeping changes to the Corporate Network that it results in the ultimate demise of our industry.

My name is Patricia A. Mott and I am President/CEO of *Arlington Federal Credit Union* in Texas, Charter #17100. The only Corporate Credit Union we use is Southwest Corporate Federal Credit Union. Southwest is *AFCU's* single source for financial services. We use Southwest for overnight deposits to clear share drafts processed through Southwest, as well as clearings for ATM, debit, ACH services, bank wires and Western Union, fed cash/coin ordering, Check 21 and branch capture, check imaging, etc. *AFCU* also invests in CD products with Southwest and has the ability to borrow on a Line-of-Credit for short-term liquidity needs.

I'm sure the very largest Natural Person Credit Unions can handle most, if not all, of these services in-house. As a small credit union of \$56 million, *AFCU* does not have the means or expertise to conduct such operations in-house, and the cost, time, and potential disruption of service to convert to other vendors is not a feasible alternative. *AFCU* highly values Southwest Corporate and would not be where it is today without the advancement in services provided by Southwest over the years at affordable pricing.

## **1. The Role of Corporates in the Credit Union System**

### Payment Systems

Payment Systems and settlement of payments as noted above are of critical importance to credit unions and should remain a major service provided by Corporate Credit Unions. Southwest Corporate is a leader in payment systems and all related settlement processes. That being said, those services require a high degree of liquidity, as credit unions need to be assured of funds available through overnight deposits and short-term loan availability.

I think Corporates that provide a broad range of Payment Systems services, have a high percentage of member credit unions utilizing those services, and have the expertise to enhance those services in an ever-changing technological environment should maintain those services as a core part of their business. The risks associated with the Payment Systems part of the Corporate can and should be addressed through improved liquidity management outlined in its policies and business plans and through improved supervision by the regulator rather than through regulation. Risks can also be mitigated through regulatory requirements that credit unions utilizing services of a Corporate must capitalize the Corporate. Finally, a Corporate that engages in these Payment Systems services can also reduce risk by modifying investment policies and strategies to maintain a higher percentage of short-term investments and enhancing their Liquidity Contingency Plans to restrict or limit borrowing unless for contingency situations.

I don't think Payment Systems should be segregated from Corporate operations or put into a CUSO or put under a separate charter. These options are totally unnecessary if liquidity management, capital, and investment terms are addressed.

#### Liquidity and Liquidity Management

Corporate Credit Unions need to address liquidity not only for Payment Systems, but also in order to fund loans to credit unions. In the case of *AFCU*, we only borrow from Southwest Corporate, and only in the event of short-term liquidity needs, usually overnight. Although I agree that NCUA should amend Part 704 to address liquidity needs, borrowing sources, cash flows, and measurement methods in stressed scenarios, I feel that NCUA should test a Corporate's liquidity policies and procedures for adequacy during its supervision examinations. It is also my hope that NCUA will succeed in its efforts to increase the statutory limit on the CLF as well as allow access to the CLF directly by Corporate Credit Unions.

#### Field of Membership

Over the years many Corporate Credit Unions have attained national fields of membership or wide geographic fields due to mergers. Although I believe a restructuring of the Corporate system is inevitable, I believe it should be allowed to evolve slowly to prevent further instability of the entire credit union system and any undue service disruptions for Natural Person Credit Unions. The national fields of membership should stay intact. A natural stabilization or reduction in growth could be achieved by requiring credit unions to capitalize the Corporates they choose to use for services and investments. The member credit unions should have a choice of belonging to any Corporate based on member eligibility, including a capitalization requirement to access any services.

I feel that natural consolidation of the Corporate Credit Unions will continue to occur. I believe NCUA should not force consolidation and should give the Corporate system time to evolve on its own through member choice. New capital requirements and regulatory amendments coming through the results of this ANPR will most likely return most Corporates to serving more of their geographic area, but that should be left to the membership.

#### Expanded Investment Authorities

Depending on the types of services a Corporate Credit Union offers and the needs of the membership, Corporates should be allowed expanded investment authorities if they qualify within the regulatory guidelines and through the supervision examination process.

Diversification of investments is critical for Corporates, but should be strictly supervised. If requirements are not met, NCUA already has the authority under 704 to restrict a Corporate's authorities. Limitations can also be established through regulatory concentration limits tied to capital. I do believe that Corporate Credit Unions with expanded authority for investments should be required to have higher capital than currently required.

#### Structure: Two-Tiered System

I think US Central is no longer needed as a wholesale Corporate Credit Union. Although it provides some services for all Corporate Credit Unions, it can probably be downsized over time and continue to provide CUSO services utilized by the Corporates. Another option could be to merge smaller Corporates, crippled by the market dislocation and the conservatorship, into US Central as a regional Corporate. However, I believe this would take many years to achieve, as investments would have to mature or be sold when the markets improve, and all Corporate Credit Unions as well as NPCUs should be given ample time to regain their capital and strength.

## **2. Core Capital**

Core Capital should continue to include only retained earnings and PIC. But, the core capital ratio should probably be doubled. They should be required to achieve an operating income to generate capital through retained earnings. As stated earlier, member credit unions should be required to capitalize each Corporate to meet eligibility to use services, and NCUA should allow a reasonable period of time for Corporate Credit Unions to attain the new levels of capital.

### Membership Capital

In order for Corporate Credit Unions to maintain the services offered and needed by member credit unions, Membership Capital Shares should be required for eligibility to use any services of a Corporate. A member credit union should also be able to capitalize more than one Corporate Credit Union if they so choose. The MCS amount should only be based on the credit union's assets, with annual adjustments based on assets. Notice for withdrawal of MCS should probably be extended to at least five years to provide more capital stability. However, there should be a phase-in period to ease the transition for credit unions, and time to allow the Corporates to fully assess the impact of investment losses. When the "dust settles" credit unions will be better able to evaluate Corporate Credit Unions and service requirements to decide which Corporate(s) to capitalize. The time period for capitalization should be long enough for credit unions that are switching services to meet all contract obligations.

### Risk-Based Capital and Contributed Capital Requirements

NCUA should implement risk-based capital requirements, utilizing weighted asset values of the various risk categories of the Corporate balance sheet.

## **3. Permissible Investments**

The investments authorized under Part 704 should not be prohibited for Corporate Credit Unions. But, the Corporate should demonstrate that it has the capabilities and resources to manage the investments. I feel that NCUA should implement regulatory concentration limits as to the amount of capital a Corporate can hold in certain investment types. Also, I would expect that reforms in response to the credit market issues would improve the quality of ratings agencies, require higher capital, and require a higher degree of regulatory oversight on ratings agencies and issuers, and that changes in risk models would be implemented.

## **4. Credit Risk Management**

Even though there should be reforms coming down from Congress and the financial regulators to address credit ratings and changes in risk modeling, NCUA should require Corporate Credit Unions to maintain staff and systems necessary to conduct internal reviews as well as third-party modeling to conduct stress tests.

In order to diversify, Corporate Credit Unions with expanded investment authorities particularly need to set policies on concentration limits for specific investments, sectors or obligors, as well as comply with NCUA-established concentration limits. If the investment function fails to comply with the regulations or internal policy limits, the credit department should have the independent authority to divest the Corporate of these investments. Corporates should also be required to document changes in credit spreads, conduct stress testing internally, and conduct third-party reviews of the process used.

## **5. Asset Liability Management**

NCUA should amend Part 704 to include the requirement of performing net interest income modeling and shock tests to project income under different scenarios to complement the NEV measurement of risk to the balance sheet.

## **6. Corporate Governance**

I believe that Boards of Corporate Credit Unions should be elected by their memberships and from within their memberships.

With the magnitude of the market turmoil affecting every type of financial institution globally, I don't believe that the make-up of the Boards could have shielded any from the impact. Whether they had term limits, were paid, were outside directors---or not---the market dislocation occurred. I feel there is no need to change the governance of Corporate Credit Unions. The member credit unions should continue to elect Board members to direct their Corporate. They are well qualified to represent their fellow member credit unions and should receive regular training on subjects relating to products, services, investments and credit, as well as a range of topics relating to credit unions and the financial industry as a whole.

**In summary**, the natural evolution that has occurred within the Corporate Network since the 1970's has had a tremendous influence on the growth of the credit union movement in this country and throughout the world. The changing needs of Natural Person Credit Unions to serve the member needs spurred this evolutionary change in the Corporate Credit Unions.

This global impact to the financial and credit markets should not result in a complete overhaul of a system that basically works. I believe that through global reforms and improved regulation and supervision, as well as Congressional changes in the CLF and now the possibility of a separate fund for Corporate Credit Union coverage, the Corporate charter can and should remain intact, of course without the need for the wholesale Corporate. It is probably inevitable that within the next 30 years, there may be only a handful of Corporate Credit Unions serving fewer Natural Person Credit Unions (through natural consolidation as well). As the needs of NPCU members change, the natural progression will be NPCU evolutionary change that will require Corporate Credit Unions to evolve to satisfy those needs. Again, I would ask that NCUA be cautious in its efforts to change Corporate Credit Unions that are so widely used and needed by Natural Person Credit Unions serving approximately 92 million consumers. The effects of a drastic change could be disastrous to our industry.

Sincerely,

A handwritten signature in black ink, reading "Patricia A. Mott". The signature is written in a cursive, flowing style.

Patricia A. Mott  
President/CEO

cc: Board of Directors, *Arlington Federal Credit Union*